International Business Environments and Operations, 13/e

Part 6

Managing International Operations



Chapter 19

The Multinational Finance Function

Chapter Objectives

- To describe the multinational finance function and how it fits in the MNE's organizational structure
- To show how companies can acquire outside funds for normal operations and expansion, including offshore debt and equity funds
- To explore how offshore financial centers are used to raise funds and manage cash flows
- To explain how companies include international factors in the capital budgeting process
- To discuss the major internal sources of funds available to the MNE and to show how these funds are managed globally
- To describe how companies protect against the major financial risks of inflation and exchange rate movements
- To highlight some of the tax issues facing MNEs

The Finance Function

Acquires and allocates financial resources among the company's activities and projects.

Four key functions are:

- Capital structure
- Long-term financing
- Capital budgeting
- Working capital management

Capital Structure

- Leveraging Debt Financing
- Factors Affecting the Choice of Capital Structure
- Debt Markets as Means of Expansion

Global Capital Markets

- Eurocurrencies and the Eurocurrency Market
- International Bonds
- Equity Securities and the Euroequity Market
- The Size of Global Stock Markets

Offshore Financing and Offshore Financial Centers

- Offshore financial centers (OFCs)—cities or countries that provide large amounts of funds in currencies other than their own.
- Characteristics
- Operational versus Booking Centers
- OFCs as “Tax Havens”

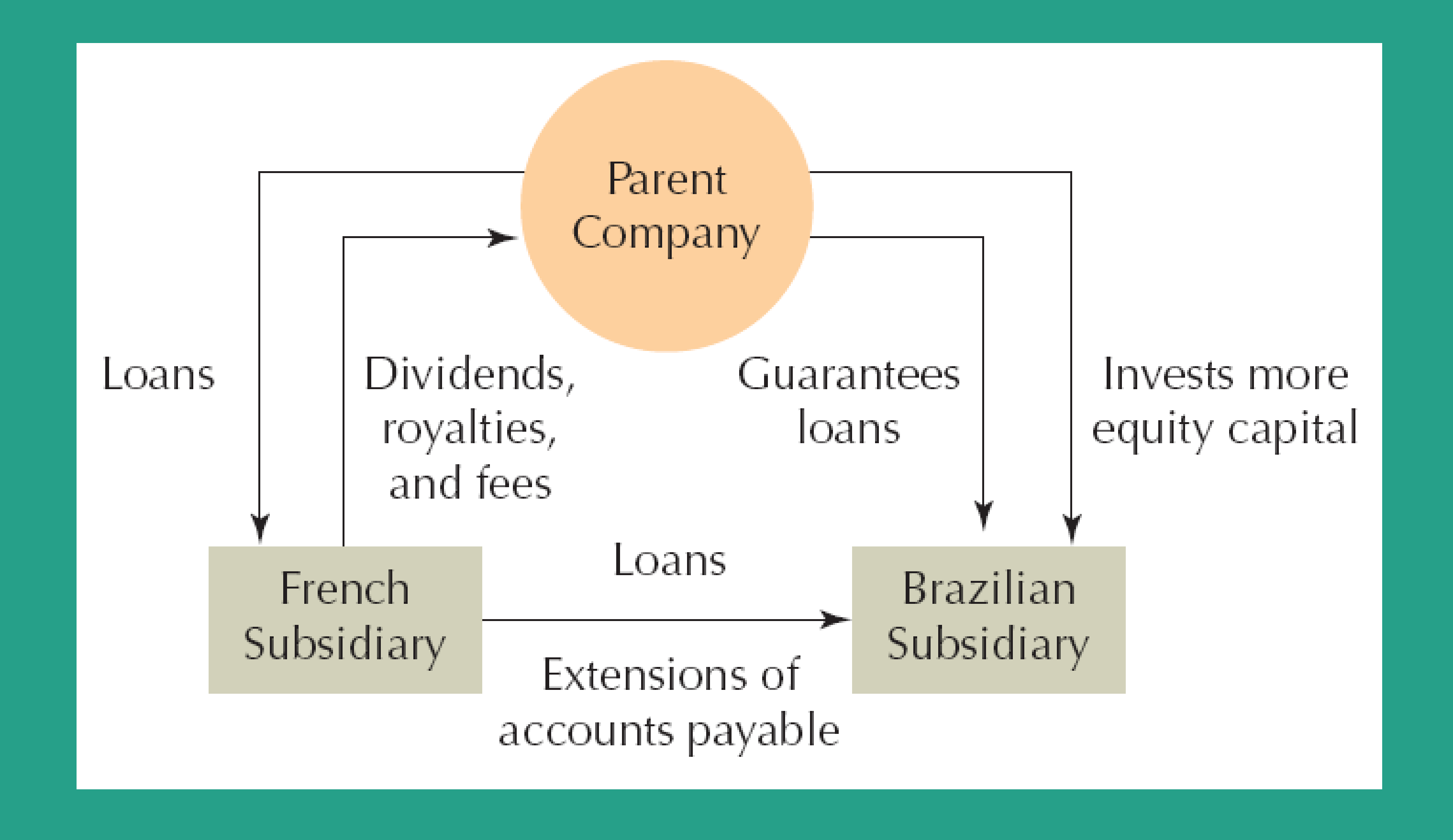
Capital Budgeting in a Global Context

- Capital budgeting—the process whereby MNEs determine which projects and countries will receive capital investment funds.
- Methods of Capital Budgeting
- Complications in Capital Budgeting

Internal Sources of Funds

- Funds are working capital, or current assets minus current liabilities.
- Sources of internal funds are
  - Loans
  - Investments through equity
  - Capital
  - Intercompany receivables and payables
  - Dividends

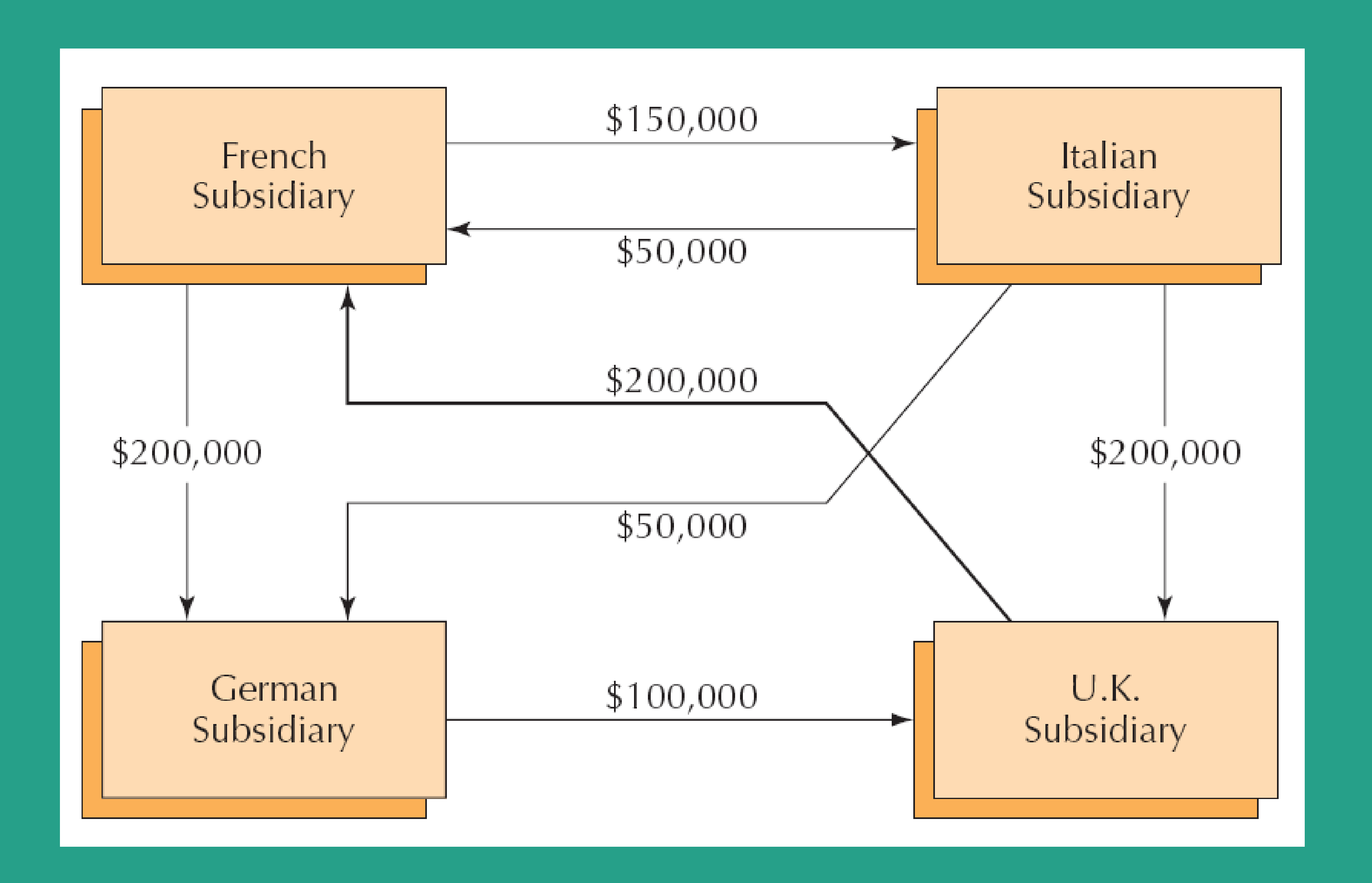
How the MNE Handles Its Funds



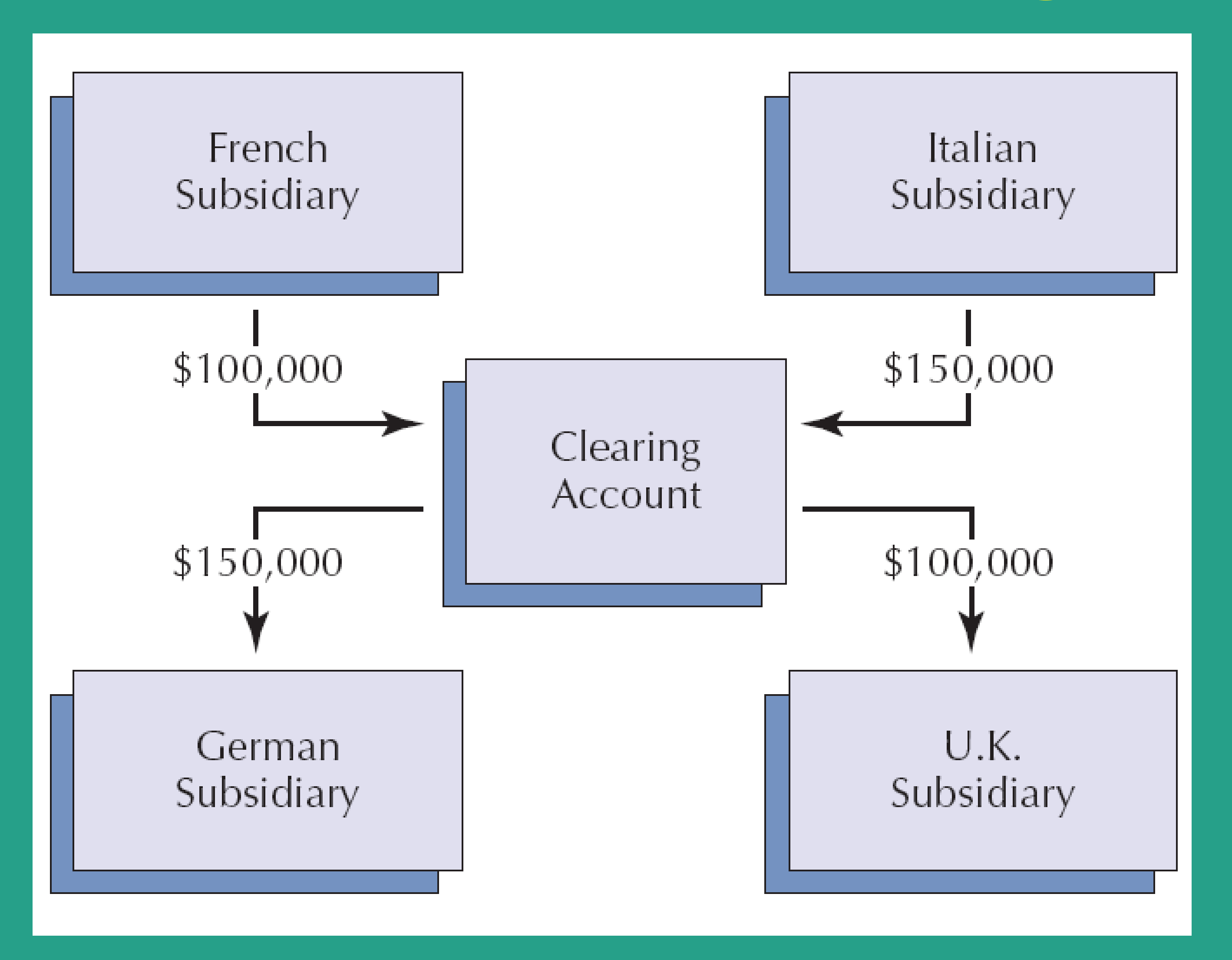
Global Cash Management

- To ensure effective cash management, CFOs must determine:
  - What are the local and corporate system needs for cash?
  - How can the cash be withdrawn from subsidiaries and centralized?
  - Once the cash has been centralized, what should be done with it?
- Multilateral Netting

Multilateral Cash Flows



Multilateral Netting



Foreign Exchange Risk Management

- Types of Exposure
  - Translation Exposure
  - Transaction Exposure
  - Economic Exposure
- Exposure Management Strategy
  - Defining and Measuring Exposure
  - Creating a Reporting System
  - Formulating Hedging Strategies

Taxation of Foreign Source Income

- International Tax Practices
- Taxing Branches and Subsidies
- Transfer Prices
- Double Taxation and Tax Credit

International Tax Practices

- Differences in Tax Practices
  - Differences in Types of Taxes
  - Differences in GAAP
  - Differences in Tax Rates
- Two Approaches to Corporate Taxation
  - Separate Entity Approach
  - Integrated System Approach

Taxing Branches and Subsidiaries

- The Foreign Branch
- The Foreign Subsidiary
- The Controlled Foreign Corporation
  - Active versus Passive Income
  - Determining a Subsidiary’s Income

Determining Subsidiary Income

U.S. Stockholder (parent company)

Foreign Corporation (non-CFC)	CFC	Foreign Branch
Income is taxable to the parent when declared as a dividend, regardless of whether the income is active or Subpart F. Deferral applies.	Active income is tax deferred. Subpart F income is taxable to the parent when earned by the CFC.	All income is taxable to the parent when earned by the branch.

Transfer Prices

- A price on goods and services one member of a corporate family sells to another.
- Transfer Prices and Taxation
  - Companies establish arbitrary transfer prices because of differences in taxation between countries.
  - The OECD is concerned about how companies manipulate transfer prices to minimize their tax liability worldwide.

Double Taxation and Tax Credit

- Tax Treaties Eliminating Double Taxation
  - The purpose of tax treaties is to prevent double taxation or to provide remedies when it occurs.

Future: Technology and Cash Flows

- Greater emphasis on moving corporate cash worldwide to take advantage of differing rates of return and minimize tax bills.
- OECD countries are trying to break barriers to bank secrecy.
- Technological innovation will allow companies to transfer funds more quickly worldwide.